IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

FIRST APPEAL No 573 of 1996

Hon'ble MR.JUSTICE Y.B.BHATT

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1. Whether Reporters of Local Papers may be allowed to see the judgements?

2. To be referred to the Reporter or not?

3. Whether Their Lordships wish to see the fair copy of the judgement?

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?

5. Whether it is to be circulated to the Civil Judge?

SWASTIK INDUSTRIAL CORP.

Versus

CENTRAL BANK OF INDIA

Appearance:

MR JD AJMERA for Petitioners

MR KK NAIR for Respondent No. 1

CORAM : MR.JUSTICE Y.B.BHATT

Date of decision: 31/07/96

ORAL JUDGEMENT

1. The appellants herein have challenged in the present appeal the decree passed by the trial court in favour of the first respondent-original plaintiff. The plaintiff bank had filed a suit against the various defendants (the appellants being original defendant nos.1 and 2) for recovery of the amount which the bank was required to pay and had in fact paid to a third party, in whose favour the plaintiff bank had issued a bank

guarantee at the instance of the defendants.

2. From the facts of the case it appears that the defendants had entered into a contract with a third party (The Tamilnadu Electricity Board) and under the terms of the contract or otherwise, the plaintiff bank had issued a bank guarantee for a specified sum in favour of the said third party at the instance of the defendant. This bank guarantee admittedly was a "performance guarantee".

3. Since the said third party had invoked the bank guarantee during the validity period of the said guarantee, the plaintiff bank was obliged to pay the specified amount, which it had in fact paid. The plaintiff bank, therefore, filed a suit for recovery of this amount in turn from the defendants. The trial court decreed the suit in favour of the plaintiff bank, and it is this decree which is in challenge in the present appeal.

4. The main thrust of the submissions made by the learned counsel for the appellants is to the effect that the plaintiff bank was not obliged to encash and/or honour the said bank guarantee in favour of the third party inasmuch as there were pending disputes between the appellants-defendants and the said third party. In view of such disputes, the said third party could not legitimately hold out to the plaintiff bank and/or profess that there was any breach on the part of the defendants in respect of "performance guarantee", and that therefore the plaintiff bank was obliged to make payment under the said guarantee. In other words, learned counsel for the appellant sought to make out a case that the plaintiff bank ought not to have permitted the third party to invoke and/or encash the said bank guarantee for the simple reason that there were disputes between the contracting parties. In other words, counsel for the appellants contends that until the plaintiff bank was satisfied that there was justification on facts, or until the plaintiff bank arrived at a decision on a question of fact that the third party was not in the wrong under the terms of the contract, the plaintiff bank was not obliged in law to make payment under the said guarantee.

5. This submission on the part of the appellants cannot be entertained in view of the well settled position in law. The trial court has discussed the same with adequate clarity on page 7 of the judgement. On my part I need not reiterate and re-discuss the entire case law on the subject. Suffice it to say that once the bank

guarantee is issued by a bank in favour of a party (in the instant case referred to as third party) and once such bank guarantee is invoked by such a third party, the bank is bound to honour the same barring a few rare exceptions on questions of fact, for example, where the validity period of the guarantee has already expired.

6. It is also a well settled principle that the bank has no concern with the disputes that may be pending between the parties, and it also has no concern nor does it have any obligation in law to decide or make up its own mind as to which of the contesting parties is right on facts or otherwise. To canvass the proposition that the bank, before honouring the bank guarantee, must decide the dispute between the parties, or that it need not in law honour the bank guarantee until such disputes between the parties are settled or decided before an appropriate forum, would frustrate the very purpose of issuing a bank guarantee, and would seriously hamper the smooth transaction of commerce.

7. Learned counsel for the appellants sought to place reliance upon a decision of the Supreme Court in the case of Larsen & Toubro Ltd. Vs. Maharashtra State Electricity Board (AIR 1996 SC 334). Learned counsel sought to rely upon the observation made in para 11 of the said decision. Having considered the same I am of the opinion that the same would not assist the appellants on the facts of the present case.

8. In the said decision the Supreme Court, considering the relevant facts of that case, concluded that the court below was in error in not issuing an injunction, and the Supreme Court therefore issued an injunction restraining the concerned respondents from invoking the bank guarantee. However, the reasons as to why the Supreme Court did not permit the invocation of the bank guarantee are relevant and germane to the issue. From a plain reading of the said decision it becomes obvious that the guarantee in question before the Supreme court was a bank guarantee whose validity period expired on the successful completion of the trial of operation, and it was an admitted position that the Board had taken over the plant after the successful trial operation and performance, etc. In other words, the validity period of the bank guarantee in question had expired once the Board had taken over the plant. It was for that reason that the Board was restrained from invoking the bank guarantee. Thus, this decision would have no application to the facts of the present case. Even otherwise, the observations made in para 4 of the said decision clearly

make out an exception to the actual facts discussed in the said decision, in respect of "bank guarantee relating to performance". The "performance guarantee" at item no.2 in the said guarantee had not been invoked, and is therefore not covered by the subject matter of the proceeding before the Supreme court. In the instant case it is a case of "performance guarantee" and for that reason also the cited decision would have no application to the facts of the case.

9. In the premises aforesaid there is no substance in the present appeal and the same is therefore dismissed. Notice is discharged with no order as to costs.

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